Uzbekistan Enacts New Tax Code

General

Uzbekistan has adopted a new Tax Code (the “New Tax Code”)\(^1\), which replaces the 2008 Tax Code. Most of the New Tax Code’s provisions are effective as of 1 January 2020.

The stated purposes of the New Tax Code include decreasing the overall tax burden, simplifying tax rules, and improving tax administration. According to Ministry of Finance, the New Tax Code has been prepared taking into consideration recommendations of the International Monetary Fund, the World Bank and other international experts.

Below we summarize some of the most important changes introduced by the New Tax Code.

1. Digital Services

With effect from 1 January 2020, non-residents of Uzbekistan are required to pay local VAT (15%) on a number of digital services provided to individual customers who live in Uzbekistan (or who use local bank accounts to pay the purchase price, have a network address registered in Uzbekistan, or use a Uzbekistan phone number to make the order). Such services include: supply of software, e-books, music and other digital content through the Internet, domain and hosting services, streaming services, platforms for online trade, online advertising services, etc. Certain types of services, however, are not covered (e.g., Internet access services and provision of consulting services via e-mail).

This change is aimed at dealing with the issues raised in the BEPS Action 1 document (i.e., the unfair competitive advantage of offshore suppliers of digital content compared to local suppliers).

Foreign suppliers of digital services are required to register as VAT payers with the Uzbek tax authorities within 30 days after the service is supplied.

The State Tax Committee has launched a website (http://tax.uz/en), where non-resident suppliers of e-services may register with tax authorities and submit reports.

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2. Transfer Pricing

The New Tax Code introduces a detailed transfer pricing regulation which will take effect on 1 January 2022. Previously there was no such regulation. Some of the main aspects of the new rules are summarized below:

(i) For tax purposes, a controlled transaction should be on market terms. There are two types of controlled transactions:

   a. a transaction between related parties with the amount exceeding 5 billion soums (approximately 524,000 USD at the current exchange rate) (in certain specific cases - 500 million soums); and

   b. cross-border transactions with oil, oil products, precious and non-ferrous metals, and certain other types of products (the full list of which should be approved by the State Customs Committee) or transactions where one of the parties is established in a designated offshore jurisdiction. These transactions may be between related and unrelated parties.

(ii) Information on controlled transactions should be submitted to the tax authorities on an annual basis.

(iii) The New Tax Code provides for a list of sources of information which should be used to determine the market price (quotations of commodity exchanges, etc.).

(iv) If the tax authorities determine that there is a deviation between the transaction price and the market price, they may adjust the transaction price accordingly and assess unpaid/underpaid taxes and impose fines and penalties. The transfer pricing rules provide for the following methods of determining market price: comparable market price method; resale price method; costs plus method; comparable profitability method; and profit split method.

(v) At the request of the State Tax Committee, the taxpayer should submit transfer pricing documentation in relation to a specific transaction (such as justification of the used price determination method). Such a request cannot be made before 1 June of the year which follows the year in which the transaction was executed.

(vi) Transfer pricing audits may be conducted only by the State Tax Committee and may be initiated generally not later than 4 years from the date on which the relevant transaction was reported.

(vii) It is possible to sign an advance pricing agreement with the State Tax Committee which sets forth, among other things, the methodology of determining the price in relation to specific products.
3. Controlled Foreign Companies

With effect from 1 January 2022, the New Tax Code introduces the concept of a controlled foreign company (a "CFC").

Under the CFC rules, a local tax resident (either a company or an individual) will generally be deemed to have a CFC if it holds more than 50% of the shares (from 1 January 2023 - more than 25%) in a foreign company unless such company (among other things):

(i) is deemed to be an active foreign holding company (according to the tests established in the New Tax Code) and is not incorporated in an offshore jurisdiction, the list of which is to be approved jointly by the State Tax Committee, the Central Bank and the State Customs Committee; or

(ii) is subject to an effective corporate income tax rate of not lower than 15% and is located in a country with which Uzbekistan has a double tax treaty.

If a local tax resident is deemed to have a CFC, it should pay income tax on the undistributed profits of such CFC in proportion to its shareholding in it.

Also, the local tax resident should submit a standard form notification to the tax authorities on its participation in any foreign company (within one month after acquisition of its shares) and in a CFC (until 20 March of the year following the year in which a CFC’s profit becomes taxable in Uzbekistan).

4. Thin Capitalization

From 1 January 2020, the New Tax Code imposes limitations on deductibility by a local borrower of “controlled debt” for its corporate income tax purposes. Controlled debt is debt owed to a related party (which includes a person or entity holding more than 20% of shares in the borrower), as well as to a lender that has obtained a guarantee or other security of repayment from a borrower’s related party.

Deduction would be allowed only for the portion of interest and penalties under controlled debt which remains after such interest (penalties) is divided by a capitalization coefficient. This coefficient, in turn, is calculated as follows: controlled debt divided by the borrower’s own capital and then divided by an indicator which is equal to 3 (13 for banks and financial lessors).

5. Permanent Establishments

The New Tax Code incorporates the following changes (among others) in relation to the rules relating to a permanent establishment ("PE"):  

(i) While previously a construction was deemed to constitute a PE from the first day of its existence, now it will constitute a PE only if it has existed for more than 183 days during any consecutive 12-month period.
(ii) Personnel secondment arrangements previously provided relief from PE status if the personnel acted on behalf and in the interests of the receiving entity. The following additional conditions have been added: the seconding entity is not liable for the work of the seconded personnel and the seconding entity's profit should not exceed 10% of its secondment costs.

(iii) A PE of a foreign company will arise not only where a person enters contracts on behalf of a company in Uzbekistan, but also where a person plays a principal role in entering into such contracts.

(iv) Previously, foreign companies were not deemed to be VAT payers, regardless of whether they had a PE in Uzbekistan. Under the New Tax Code, foreign companies operating through a PE are considered VAT payers.

6. VAT

The following changes have been introduced in relation to VAT (among others):

(i) VAT invoices now are generally issued only in electronic form.

(ii) Before the New Tax Code, an excess of input VAT over output VAT was refundable by the state only to VAT payers which have sales that are subject to zero rate VAT (such as exporters). Under the New Tax Code, from 1 July 2020, all VAT payers have the right to request the refund of such excess. The refund requires a chamber audit by the tax authorities and should generally be performed within 60 calendar days from the date of the refund claim (for certain categories of VAT payers - within 7 days).

(iii) Previously, when a VAT payer acquired works or services which are subject to VAT from a foreign supplier, the VAT payer had to pay VAT in relation to such works and services from its own funds. Under the New Tax Code, if any local taxpayer (regardless of whether it is a VAT payer) acquires services from a foreign supplier which is not registered as a VAT payer, the local taxpayer should withhold VAT from the amount of services paid to the foreign supplier.

7. Other Changes

Other significant changes introduced by the New Tax Code:

(i) Under the New Tax Code, the maximum period for a carryforward of income tax losses is 10 years (previously - 5 years), and the maximum amount of the loss that may be carried forward is 60% of the tax base (previously - 50%).

(ii) Effective from 1 January 2022, the New Tax Code introduces the possibility of creating a consolidated group of taxpayers for purposes of paying income tax in relation to the combined result of their operations.
(rather than individually by group members). This is possible only if certain strict conditions are met (e.g., at least 90% of the shares in each group member are owned by the same company, the total sales of all group members should be at least 500 billion soums (approximately 52,400,000 USD), and the total amount of VAT, excise, income tax and subsoil tax paid by them should be at least 100 billion soums). These restrictions make the tax consolidation option available only for a very few taxpayers.

(iii) Tax incentives provided by the previous Tax Code will remain in effect only until 1 April 2020. However, the incentives granted by Resolutions of the President and the Cabinet of Ministers will continue to apply for the periods indicated in such Resolutions.

(iv) Going forward, any tax incentives generally may be provided only in the New Tax Code. As an exception, the President may grant tax incentives (except in relation to VAT, excise and subsoil taxes), but only in the form of a tax rate reduction of not more than 50% and for a term not exceeding 3 years.

(v) Companies with foreign direct investments operating in priority areas/projects are exempt from land tax, property tax and water use tax for the period stipulated by Resolution of the President.

(vi) A taxpayer may apply an “investment deduction” in the form of the following accelerated depreciation of fixed and intangible assets:

- 10% of the cost of new technological equipment, expenses for modernization of production and/or the amounts allocated for the purchase of domestically produced software as part of investment projects to create information systems (such depreciation may be taken in the year in which the equipment is commissioned and modernization or purchase is completed); and

- 5% of the amounts allocated for expansion of production in the form of new construction, reconstruction of buildings and structures used for production needs (such depreciation may be taken in the year in which the expansion is completed).

(vii) State duties and bonuses for subsoil use are not included in the New Tax Code and are now regulated by separate laws. Under the amendments to the Law "On Subsoil" which were made in connection with the New Tax Code, the rates of the subscription bonus were generally reduced by two times.

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Certain taxes and obligatory payments have been renamed, such as:

- what was known as the unified social payment is now the social tax;
- the previous unified tax payment is now called the turnover tax.

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